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**DEPARTMENT OF DEFENSE**  
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IN REPLY REFER TO

PAS 2-730.3a

May 14, 2002  
02-PAS-039(R)

**MEMORANDUM FOR REGIONAL DIRECTORS, DCAA**  
**DIRECTOR, FIELD DETACHMENT, DCAA**

**SUBJECT:** Audit Guidance on Reviewing for Fraud Risk Indicators While Planning  
and Performing the Audit

**Summary**

Based on recent comments from the field, we are providing additional guidance on reviewing for fraud risk indicators while planning and performing the audit. Specifically, a preliminary audit step has been modified or added to all applicable audit programs. This step directs auditors to review the principal sources for fraud risk indicators (e.g., CAM Figure 4-7-3, DoDIG Handbook on Fraud Indicators for Contract Auditors) and become familiar with specific fraud indicators applicable to the type of audit they are performing. The handbook is hyperlinked in the preliminary audit step.

Based on this review, the auditor should assess the risk of fraud. If no fraud risk indicators are identified, this should be documented by referencing working paper B next to the audit program step and including a statement on working paper B saying the fraud indicators were considered and none were identified. If fraud risk indicators are identified, this should be documented in working paper B as well as your response/actions to the identified risks, including any additional audit steps to be performed.

**Background**

MRD 98-PAS-044(R), *Audit Guidance on SAS No. 82, "Considering Fraud in a Financial Statement Audit,"* was issued on March 26, 1998 to provide minor changes to DCAA guidance on fraud risk assessment and documentation procedures. SAS No. 82 requires auditors to assess the risk of fraud both in the planning stage of the audit, as well as during the performance of the audit if fraud risk indicators are disclosed. To incorporate the requirements of SAS 82, certain audit programs were updated to include a preliminary audit step to assess the risk of fraud. That step was designed to focus the auditor's attention on relevant fraud risk considerations specific to the type of audit being performed and to remind the auditor to document the consideration of fraud risk in the working papers.

## Guidance

For all audits, auditors should assess the risk for material misstatement due to fraud and should consider that assessment in designing the audit procedures to be performed (CAM 4-702.3b). Effective with the April 2002 DIIS/APPS update, all applicable audit programs will contain a preliminary audit step requiring the auditor to assess the risk for fraud. This preliminary audit step clarifies procedures to be performed regarding the review and consideration of fraud risk indicators. The preliminary audit step requires the auditor to review the principal sources for fraud risk indicators (e.g., CAM Figure 4-7-3, DoDIG Handbook on Fraud Indicators for Contract Auditors) so that auditors are familiar with the specific fraud indicators to assess the risk of fraud in the audit being performed.

If no fraud risk indicators are identified while planning and performing the audit, the auditor should reference the fraud risk indicator sources that he/she considered and include a statement that no fraud risk indicators were identified. This should be done in working paper B. An example note may read as follows:

“Based on my knowledge of the fraud risk indicators referenced in the preliminary audit step, no fraud risk indicators were identified.”

If fraud risk indicators are identified either during the planning stage of the audit or while performing the audit, the auditor should document the identified fraud risk indicators in working paper B and his/her response/actions to the identified risks (either individually, or in combination). The response/actions should note any additional audit steps to be performed. An example note may read as follows:

“Considered the fraud risk indicators referenced in the preliminary audit step. For progress payment audits, the “DoDIG Handbook on Fraud Indicators for Contract Auditors” lists several indicators for improper billing of costs. Based on audit leads in the permanent file, the contractor, on numerous instances, has been unable to provide supporting documentation for billed material cost or has provided copies of the documentation rather than the originals. Both of these scenarios are listed in the above referenced document as fraud risk indicators. Therefore, as part of the scope of this audit, we will expand the sample of verification of billed material costs to actual invoices. Also, the following additional audit steps will be performed (See working paper D-1):

- Request shipping documents to support deliveries already made to the government (to support the estimate at completion calculation).
- Check the contractor’s schedule for aging of payables back to the actual checks and invoices to determine that the dates match the supporting documentation.”

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**Concluding Remarks**

Field audit office personnel should direct any questions regarding this memorandum to their regional offices. Regional personnel should direct questions to Kenneth W. Anderson, Program Manager, Auditing Standards Division at (703) 767-3274, fax (703) 767-3234, or e-mail at dcaa-pas@dcaa.mil.

/Signed/

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